

Lanka Rest Houses Limited - 2020

1. Financial Statements

1.1 Disclaimer of Opinion

The audit of the financial statements of the Lanka Rest Houses Limited ("Company") for the year ended 31 December 2020 comprising the statement of financial position as at 31 December 2020 and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with provisions of the National Audit Act No. 19 of 2018. My comments and observations which I consider should be report to Parliament appear in this report.

I do not express an opinion on the accompanying financial statements of the Lanka Rest Houses Limited. Because of the significance of the matters discussed in the Basis for disclaimer of opinion. Section of my report I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

1.2 Basis for Disclaimer of Opinion

My opinion is disclaimed base on the matters described in paragraph 1.5 of this report.

I Conducted my audit in accordance with Sri Lanka Auding Standards (SLAuSs), my responsibilities, under those standards are further describes in the Auditor's Responsibilities for the Audit of the financial statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide basis for my disclaimed opinion.

1.3 Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards, and for such internal control as management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intend to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Company is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared of the Company.

1.4 Audit Scope (Auditor's Responsibility for the Audit of financial statements)

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional scepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible, and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to enable a continuous evaluation of the activities of the Company, and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Company has complied with applicable written law, or other general or special directions issued by the governing body of the Company
- Whether the Company has performed according to its powers, functions and duties; and
- Whether the resources of the Company had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

1.5 Audit Observations on the preparation of financial statements

1.5.1 Internal Control over the preparation of financial statements.

Entities are required to “devise & maintain” a system of internal accounting controls sufficient to provide reasonable assurance that , transactions are executed in accordance with management’s general or specific authorization, transactions are recorded as necessary to permit preparation of financial statements in conformity with the applicable reporting standards , and to maintain accountability for assets, access to assets is permitted only in accordance with management’s general or specific authorization, and the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

1.5.2 Non-Compliance with Sri Lanka Accounting Standards

Non Compliance with the reference to Particular Standard	Management Comment	Recommendation
(a) In accordance with section 6 of Sri Lanka Accounting Standard No 01, Items that use in the supplying of goods and services, held for giving to the tax base and having a physical exitance used for administrative purposes as property and equipment and in accordance with para 05 of Sri Lanka Accounting Standard No 40, land and buildings held for the purpose of earning rent or for capital appreciation should also be reported the financial statements as investment property. the company had not been identify the basis of using as property plant and Investment properly in the financial statements. In year 2010 this company had been given responsibility for running operating activity of 31 rest houses through the Urban Development Authority. Out of this, Management of 23 rest houses had been assigned to the private sector as at 31 December 2020 and 07 rest houses were inactive. Although, one rest house is being operated by the company itself,	Here, although the operations of the rest houses are carried out by the company, it's properties (Land and building) are not owned by the company. Those assets are the property of the Urban Development Authority and only its administrative activities are carried out by the company.	The basis of use of the asset should be identified and the assets should be accounted for as per the provisions of the relevant standards.
(b) In accordance with section 32 of Sri Lanka Accounting Standard No 1, although assets and liabilities should not be off set unless permitted by an accounting standard, according to financial statements of the year under review, the debtor's debit balance amounting Rs. 19.74 million had off set against the debtor's credit balance amounting to Rs.5.25 million, so the current assets and current liabilities were understated in the statement of financial position as on the last day of the year under review.	A debit balance amounting to Rs. 5,321,885 is stated to be understated. There is a difficulty to find the needed information to give answers about that amount. Because of that, it will be investigated and necessary actions will be taken.	Debit balances and credit balances should be presented separately in the financial statements as per the standard to reflect the actual position of the company's assets and liabilities.

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| <p>(c) In accordance with section 86 of Sri Lanka accounting Standard No. 37, Although the potential impact of contingent liabilities on the company's financial position or performance should be disclosed in the financial statement. The legal proceeding initiated by the company against the person who obtain the management basis of Weligama rest house from November 2009 to November 2017 and legal proceedings initiated against the company by the person who obtain the old Negombo rest house on a lease basis from November 2009 to November 2017 also had not been disclosed in the financial statement</p> | <p>Attention will be paid to those matters and efforts will be made to correct those matters in the financial statements in the future.</p> | <p>According to the standard, the status of all contingent liabilities and assets as at the end of the financial year should be disclosed in the financial statement</p> |
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1.5.3 Accounting Deficiencies

Audit Issue	Management Comment	Recommendation
<p>(a) As mentioned in the Auditor General's report of the year 2019, the capital expenditure amounting to Rs.3.19 million spent on the renovation of the Mahiyanganaya rest house, which is directly controlled by the company, had been written off against the profit of that year and had not been corrected during the year under review. Also, a total amounting to Rs. 10.42 million had been spent on the renovation work of the rest house as at 31 December 2020 but, after the completion of the renovation work, it was not recognized as an asset and it had been stated as capital expenditure under property plant. Also, Rs. 0.21 million had been depreciated for the year ended 31 December 2020 for maintenance expenditure.</p>	<p>Those values in the statement of financial position will be made correct in the future.</p>	<p>The method of reorganizing Capital Expenditure should be disclosed in the financial statement.</p>

- (b) Although the contractual Management fee income for the year under review should be amounting to of Rs.45.46 million, that income had been stated as amounting of Rs.17.09 million in the financial performance statement. It was observed that the frees to be paid to the local authorities for the use of rest house land. Which was 65 percent of the management income, had been deduct from the management fee income. Due to this, it was observed that the income and expenditures included in the financial statements had been understated by approximately Rs. 28.80 million.
- Those values in the statement of financial position will be made correct in the future.
- Management fee income and rent expenses of local authorities should be correctly identified separately and presented in the financial statements.
- (c) As per the statement of financial position of the company as at end of the year under review, the carrying value of property, plant and equipment was amounting to Rs. 13.34 million. However, it was observed that only the fixed assets purchased by the company after, the year 2012 had been included in the fixed assets schedule submitted to the audit. Accordingly, prior to 2012, Action had not been taken to identify the fixed assets in the rest houses and include them in the accounts.
- It is difficult to give a correct answer as we can not find an accurate report with values about the company's assets after the year 2012.
- The assets existing at the time of taking over the rest houses should be documents and duly taken over.

1.5.4 Unreconciled Control Accounts or Records

Item	Value as per Financial Statements (Rs) million	Value as per corresponding Records (Rs) million	Difference (Rs) million	Management Comment	Recommendation
(a) Current Account with Urban Development Authority	64.42	76.99	12.5	It will be corrected, after making a discussion with the Urban Development Authority and Company	Relevant comparisons should be made immediate and specific time in the future.
(b) Current Account	9.48	7.88	1.60	Those values in the statement of financial position will be made correct in future.	The reasons for the changes should be identified and corrected
(c) Payable to local authorities	39.26	38.70	0.56		
(d) Receivable from rest houses control by the company	18.40	19.75	1.35		
(e) Refundable tender deposit	0.12	2.59	2.46		

1.5.5 Documentary Evidence not made available for Audit

Item	Amount (Rs) million	Evidence not made available	Management Comment	Recommendation
(a) Adjustment by Journal	53.45	Supporting evidence and details relating to the relevant Journal entries.	These corrections will be implemented from the beginning of 2023.	Supporting evidence should be filed when applying journal entries.
(b) Payable cash balance to local authorities, provisions for bad debts, receivable from Weligama, Hambantota and Mahiyanganaya rest houses, Annual Depreciation etc	50.46	Detailed schedules age analysis, schedules of bad debt calculation conformation letters, schedules of Depreciation calculation respectively	Relevant financial adjustment will be made.	The relevant documents should be submitted to the audit for verifying the correctness and completeness of balance included in the financial statement

1.6 Accounts Receivable and Payable

1.6.1 Payables

Audit Issue	Management Comment	Recommendation
It was observed that payable service charge balance from 2016, amounting to Rs. 1.79 million included in other creditors and the company had not been taken action to paid that service charge during the year.	Comment had not been given.	The relevant service charge should be settled to respective parties.

1.7 Non-Compliance with Tax Regulations

Audit Issue	Management Comment	Recommendation
Although the payee tax should be remit before the 15 th of Next Month according to section 83 of Inland Revenue Act, No 24 of 2017 payee tax amounting to Rs.550,236 for the year 2019 had not been remitted as at 31 December 2020.	In this regarded, action will be taken in the future.	The responsibility of the company is to pay the statutory obligations as due.

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs.3.77 million and the corresponding profit in the preceding year was amounted to Rs. 8.61 million. Therefore, a deterioration to Rs. 4.85 million of the financial result was observed. The main reason for the deterioration was decrease of income by Rs.6.72 million that is an equivalent of 50 percent.

2.2 Trend Analysis of major Income and Expenditure items

Items	Year under review (2020) Rs. Million	Responding Year (2019) Rs. Million	Difference Rs. Million	Percentage of difference
Rest House Income	2.68	5.38	(2.7)	(50%)
Interest Income	4.84	6.03	(1.19)	(19.73%)
Salary and Wages	6.98	4.56	2.42	53%

2.3 Ratio Analysis

Ratio	Year under review 2020	Corresponding year 2019	In difference Percentage
Gross Profit Ratio	90.70%	88.74%	1.96%
Net Profit Ratio	24.17%	36.60%	(12.43) %
Current Ratio	0.72	0.66	0.06
Quick Assets Ratio	0.72	0.66	0.06

Although, the current ratio should be at least 02 current assets to 01 current liability for having desired liquidity level of an entity. The Corresponding year and year under review, it had been a very low level of 0.66 current assets for 01 current liability. It was observed the reason for that the amount to be paid to the local authorities was very high.

Although, the Quick ratio should also be at least 01 current assets to 01 current liabilities, It was lower that for the corresponding year and year under review. It was also observed that this had been very adverse effect on the short-term liquidity of the Company.

3. Operational Review

3.1 Management Inefficiencies

Audit Issue	Management Comment	Recommendation
(a) Base on the Gazette notifications No 105/3 dated on 09 September 1980 and 170/8 dated 11 December 1981, 38 rest houses own by local Authorities had been vested to Urban Development Authority and According to the decision made by the Cabinet of Ministries on 17 July 2006, administration of that rest house had been vested to the company . Although the cabinet of ministers had decided that the assets including rented assets and good will to brought to the first balance sheet, to appoint a private management agent and to revalued all the assets including good will. However, this decision had been implemented until now.	Comments had not been given	According to the decision made by the cabinet on 17 July 2006, relevant assets should be revalued and entered in to financial statements.

- (b) The audit observed that the managers of the 03 rest houses where in Beruwala, Matale and Kataragama had been violated the agreement before ended up the contract period. the actions taken by the company against the rest house management due to violate the agreement had not been disclosed to the audit. Comments had not been given Action against violations of agreements should be expedited.
- (c) According to agreement entered into with each rest houses, the bade rest house should submitted audited annual financial statement to the company on or before 31 October of the following accounting year. However, none of the rest houses manage by private sector had not been submitted audited annual financial statement as per the agreements as at date of this report. But the company had not been taken necessary action regarding the violation of condition of the agreement. Comment had not been given. Action should be expedited against violations of agreements.

3.2 Transactions of Contentious Nature

Audit Issue

Written evidence had not been submitted to the audit in respect of decision to pay to the local authority 65 percent of the monthly Management fee income received from owned by local authorities and currently administration by the lanka rest houses company.

Management Comment

Comments had not been given.

Recommendation

The decision relating to the above payment and written evidence should be submitted to audit.

4. Accountability and Good Governance

4.1 Submission of Financial Statement

Audit Issue

Although, annual financial statements of the company should be submitted for audit on or before 28 February of the following year, the financial statement of the year under review had been submitted to the audit only on 02 November 2022.

Management Comment

Comments had not been given.

Recommendation

The financial statements should be submitted to the audit on due date.

4.2 Corporate Plan

Audit Issue

A corporate Plan had not been Prepared for the company to cover the year under review.

Management Comment

Comments had not been given.

Recommendation

Should be prepared and approved by the Board of Directors.

4.3 Annual Action Plan

Audit Issue

Annual Action Plan for the year under review had not been prepared.

Management Comment

Comments had not been given.

Recommendation

An annual Action Plan for the year under review should be prepared and approved by the board of directors before starting year.

4.4 Budgetary Control

Audit Issue

A budget for the year under review had not been prepared.

Management Comment

Comments had not been given.

Recommendation

As a control tool an annual budget for each financial year should be prepared and obtained approval from the board of directors before the commencements of the year